

MINUTES
BOARD OF TRUSTEES OF THE
PUBLIC EMPLOYEES' RETIREMENT FUND
143 West Market Street, Suite 500
Indianapolis, Indiana 46204
November 16, 2005

REGULAR SESSION

Board Members Present

Ken Cochran, Chair
Chuck Schalliol, Vice Chair
Kathy Ettensohn
Matt Murphy
Bob Welch

Board Members Absent

Regina Overton

Others Present

Tony Armstrong, Office of Management & Budget
Doug Todd, McCready & Keene
Richard Lenar, McCready & Keene
Elaine Beaty, McCready & Keene
Iliana Nikolova, Mercer Investment Consulting
Greg Strack, State Budget Agency
Bill Huillier, Great West

PERF Staff Present

David Adams, Executive Director
Bruce Fink, Chief Investment Officer
Charles Johnson, Chief Financial Officer
Terren B. Magid, Chief Operating Officer
David A. Huffman, Chief Technology Officer
Michael Henning, Human Resources Director
Jeffrey Carter, Director of External Affairs
Andrea Unzicker, General Counsel
Linda Villegas, Staff Attorney
Jayelynn Willman, Executive Assistant to the Board

Meeting called to order at 12:04pm by Chairman Cochran.

I. Approval of Minutes

MOTION duly made and carried to approve the minutes from the September 16, 2005 board meeting.

Proposed by: **Chuck Schalliol**
Seconded by: **Matt Murphy**
Votes: **5 in favor, 0 opposed, 0 abstentions**

II. Board Fiduciary Liability Discussion

Chairman Cochran stated that at last month's meeting the board received information from Linda Villegas on the fiduciary liability insurance.

Ms. Villegas stated that it is the opinion of the PERF legal staff and the Executive Director that the board and all fund employees are protected under the Indiana Tort Claims Act by the public employee definition within the Act.

Ms. Villegas also stated that it is the opinion of the PERF legal staff and the Executive Director that the coverage provided by the Indiana Tort Claims Act is adequate because the types of claims that would not be covered under the Indiana Tort Claims Act would not be covered by other fiduciary liability insurance.

The board members agreed with staff recommendations and would not be seeking additional fiduciary liability insurance.

III. 1st Quarter 2006 Investments Update

Bruce Fink provided the board an investment update for the quarter ending September 30, 2005. The CRIF had assets of \$12.994 billion outperforming the benchmark by 0.7%.

Mr. Fink stated that all major asset classes out performed their benchmarks for the first quarter except for fixed income. Investment staff continues to have some concern with mid-cap domestic equities and will continue to monitor.

Mr. Schalliol noted that it appears Wells Capitol Management is performing well and that Brandes Investments Partners seems to be underperforming.

Mr. Fink explained that over the short term Brandes has been trailing, but that since it's inception they are still out performing their benchmark by around 300 bases points a year.

Illiana Nikolova from Mercer, PERF's general investment consultant, stated that Mercer is very comfortable with Brandes track record and recommends no action at this point.

Mr. Fink stated that the market did not do well in October and returns for the CRIF show a 2.17% loss. That loss was very broad across the market. Ms. Nikolova noted that the numbers we've seen thus far for November have been very strong.

Mr. Schalliol asked Ms. Nikolova the percentage of the CRIF assets in fixed income and if the fund was on target. Ms. Nikolova explained that as of October, 27% of the CRIF assets were in fixed income.

Mr. Adams explained that PERF's policy range for fixed income is currently 24-42% of the total fund with a target of 30%. One item that was discussed in previous board meetings was conducting a new asset/liability study.

Bob Welch noted that the current allocations were decided upon two years ago and that it would be a good idea for the board to review the allocations.

Kathy Ettensohn inquired if the alternative investments the board approved at the last meeting were included in this update. Mr. Fink stated that they were and indicated that the Oaktree opportunity closed on September 28th and the Lexington Partners opportunity has been signed, but the fund has not officially closed. Mr. Fink also updated that the Russell 1000 Index transition was completed on October 31st.

Matt Murphy asked Mr. Fink if it would be possible to see more detail regarding alternative investments. Mr. Fink noted that he would have his team put something together for the board.

IV. Administrative Issues

Mr. Fink explained two administrative issues that needed to be discussed and voted on by the board.

The first item was a result of the Russell 1000 transition. A portion of the assets, attributable to the ASA and Pension Relief, remained in a separate S&P 500 Index Fund. BGI, who manages this process, has asked PERF to transfer the remaining funds from a separate to a commingled account for administration purposes. There would be no additional charges.

The second item allows JP Morgan to convert foreign funds, received when PERF terminated international accounts, to US dollars. The US dollar equivalent of the foreign dollars is approximately \$45,000.

MOTION duly made and carried to approve the move of the ASA Defined Contribution Plan and the Police & Fire Pension Relief Fund to a BGI co-mingled account and to allow JP Morgan to convert the foreign currency into US dollars.

<i>Proposed by:</i>	<i>Kathy Ettensohn</i>
<i>Seconded by:</i>	<i>Matt Murphy</i>
<i>Votes:</i>	<i>5 in favor, 0 opposed, 0 abstentions</i>

V. 1st Quarter 2006 Financial Update

Dave Adams introduced Terry Magid, the new Chief Operating Officer at PERF.

Charles Johnson presented a financial update for the quarter ending September 30, 2005 and indicated there was 4.16% changed in net assets and highlighted pension relief, employer contributions and expenditures.

Doug Todd, McCready & Keene, explained that accumulated assets are anticipated to be exhausted around 2012. For 2005, the fund brought in \$62 million, but had \$100 million going out.

Mrs. Ettensohn asked what the funding requirement is once the accumulated funds run out. Mr. Johnson explained that it is set by the legislature.

Mr. Murphy asked if this was discussed with the Pension Management Oversight Commission. Mr. Adams explained that this topic was discussed and that Mr. Todd specifically presented studies for funding.

Chairman Cochran inquired as to how the funding is determined for the cities and towns. Mr. Johnson explained that a statutory formula is used to compute distribution. Mr. Todd added that it is designed to help those with the most need.

Mr. Johnson highlighted the total net assets is \$13.8B, an increase of \$421M over the quarter.

Mr. Johnson highlighted the employer contribution for the 77 Police and Fire Fund.

Mr. Johnson reviewed the administrative expenses of the fund and discussed the issues with the monthly budget and expenditures.

Mr. Schalliol expressed that he thinks it is great that PERF is providing the board with a breakdown of expenses in this manner.

VI. Audit Update

Mr. Johnson stated that the financial statements for PERF were delivered to the state office for inclusion in the state CAFR on October 28th. PERF has a preliminary meeting with the SBOA scheduled for November 21st to discuss their findings and to determine next steps towards a final exit conference.

Mr. Adams expressed that the FY 2005 exit interview took place on April 20th, 2005 giving PERF very little time between the end of that audit and the start of the current audit. PERF is very excited about being five months ahead of schedule compared to audits conducted previously.

VII. CEM Presentation

Mr. Adams explained that PERF had contracted with CEM previously to conduct a survey for FY 2004. The output of this survey compares PERF with other public pension funds. Even though the data is dated, it will still provide insight into what other systems are doing in the areas of customer service. Mr. Adams indicated that he and several members of the executive staff went on a site visit to the Texas Retirement System, considered to be one of the top systems relative to customer service. The executive team was able to validate PERF's plan for customer service initiatives.

Bruce Hopkins from CEM, provided a company background and went through a presentation that was provided in the board book. He indicated that PERF is one of the most complex systems and has a lower customer service score than other pension systems. He indicated that PERF scored low in pension inceptions which is the length of time after retirement to when a retiree receives that first check.

VIII. Benefits Update

Mr. Adams noted that the discussion would focus on operational issues and to provide the board with a good understanding of the current environment. Mr. Adams asked Terry Magid and Dave Huffman to discuss the retirement process. The intent is to walk through the

process that was in place prior to March 2005 and the current process and changes.

Mr. Magid walked the board through the retirement process prior to March 2005. Mr. Magid explained each of the processes and the operational challenges within each area.

Ms. Ettensohn asked if the current SIRIS system is considered a current, up-to-date system. Mr. Adams indicated that the technology will be considered obsolete in 2007, but in terms of functionality, management believes the system is capable of doing what is necessary but the number of manual processes around the system must be removed. Mr. Adams also indicated that there are a number of data issues that must be addressed regardless of the system that is in place.

Mr. Huffman discussed the current processes and the changes that have been made. Mr. Huffman noted that most of the changes PERF made were in three areas. The first area was to obtain audit ability and accuracy. The second area was to create a standardized process for reviewing and processing applications. The third piece was getting a handle on processing times. The first big change PERF made was to moving the pre-audit function. This process previously took 90-120 days; it's now down to 48 hours.

The second major change PERF made was to add a Service Credit Team. This team certifies all employment for every retirement application. The forms and data collection process were re-engineered as well.

PERF initiated a process to create a Final Benefit Audit. This new process allows PERF to pay benefits faster and to make adjustments once final wages are received.

Mr. Schalliol expressed that members are going to be upset if their benefit goes down. Mr. Adams noted that a letter goes out with the first payment stating that an adjustment will be made in the future.

Mr. Huffman also noted that under the old system in order for a member to receive their ASA money they had to wait until their first benefit check was issued. PERF now provides the option to receive the ASA in a lump sum or partial payment.

PERF has also created a data clean up team. There are many data issues but one of the largest with data clean up is bulk records. PERF has 58,000 bulk records. When the prior administration did the system

conversion a few years ago, disk space wasn't cheap, so a decision was probably made to roll data for many years into one record. Unfortunately, the conversion validation of the data didn't occur and in many cases the records are incorrect and additional data must be sought. PERF is now going to fix this issue and submit an RFP soon to get some help in dealing with that issue.

Mr. Adams noted that under the old process PERF had to wait until wages and contributions came in at the same time as the last day in pay status. Another enhancement implemented is to break that process into two steps. The first step is for the employer to tell PERF when someone is retiring and the final wages can come in at a later date.

Another item that was not happening previously, which also counted towards the number of errors being made, was that PERF was not auditing benefit payments consistently or uniformly. PERF has now implemented a process, which is time consuming, but ensures that 100% of all benefit payments are being reviewed under a consistent manner and then being processed for payment.

Mr. Huffman went over some of the document changes PERF has made. PERF revised the retirement application; it went from 16 pages to 7 pages. The refund application used to require four signatures and is now down to one. Checklists have been created for retirement and disability applications to help the processors insure that they do everything that needs to be done. A checklist has been developed that is now included in the retirement application detailing to the member what needs to be included with the application. Mr. Huffman also discussed changes implemented with respect to PERF's business intelligence. PERF is developing a reporting wrapper around the system. PERF had not previously been using any of the system generated reports. In the current system, you cannot generate certain reports because a status field, over time, has been corrupted. PERF has been building a reporting system that can do those reporting functions for us. Metrics are now being developed to understand our production numbers.

PERF's imaging system went through a major upgrade to make the system response time faster as well. Mr. Huffman and his team installed the last 5-6 releases that had not been previously installed. Much testing went into this process. By the end of 2005, PERF should see a dramatic increase in the speed of the system.

With the help of another state agency, PERF is developing financial reports.

PERF is also developing a microfiche document retention policy and working with the state to help implement it.

Mr. Adams also indicated that the state is implementing the PeopleSoft Financial System and PERF will be adopting and implementing this system as well.

PERF is now in the process of re-implementing SIRIS. PERF is going to take the manual processes and calculations that happen outside of the system and program them back into the system.

On July 1st of this year the state legislature gave both boards of TRF and PERF the ability to value the ASA accounts on something other than a quarterly basis. PERF can value these on a more dynamic basis, as short as daily if so desired. PERF plans on presenting recommendations in the future and what changes may be required.

It has been identified that the existing disaster recovery program is insufficient for PERF. Mr. Huffman is working on putting a disaster recovery plan in place.

PERF is going to issue an RFP to review the overall security of operations as well.

Mr. Adams indicated that PERF is planning to issue an RFP to assist with microfiching records and a RFP to assist with adjusting benefit payments.

IX. Pension Management Oversight Commission (PMOC)

Mr. Adams discussed the purpose of the commission. Mr. Adams communicated that the commission had three meetings and PERF participated in all of the meeting. Copies of the meeting minutes as well as drafted proposed legislation are included in the board books for review.

Human Resource Overview

Mr. Adams introduced Michael Henning, PERF's new Director of Human Resources. One of the scorecard goals is HR development and the implementation of a performance management system.

Mr. Henning noted that for PERF to make significant changes and advances in achieving our goals and improving their customer service they should do a better job of not only maximizing their technology

changes, but also improving what their people do and how they do it. To ramp up the performance of their associates they have to give them something to shoot towards. Right now those things are not in place. PERF is in the process of developing metrics for each function within the organization. The vehicle PERF is going to use to address the changes is called Performance Management. A lot of companies use this system; it will be designed for PERF's particular needs, but it is a system Mr. Henning has used before. Through this system PERF is going to develop and install metrics to measure and manage departments and individual performance. Using those metrics PERF will recognize and reward our performers and identify and manage any non-performance issues. PERF will also use the system to identify and prepare our high potential people for more responsible roles. There is currently no way to determine who those people are or who they might be if given the chance. Lastly PERF is going to create a salary structure that will facilitate paying associates relative to their value and contribution to the organization. Right now the system has been kind of a patchwork of things that have happened over the years and it tends to make us pay everybody in a group the same. PERF wants to change that so that there is a range that someone in a group can earn more money if they are in fact out performing their peers.

The overriding purpose of all of this is to establish and perpetuate a culture of productivity and individual achievement vs. a culture of inertia and conformity. PERF presently has very little in the way of individual performance metrics and only a little more in departmental performance metrics. There are things in the works as we speak. PERF is going to initiate this in a group setting next week. PERF is going to start out with group or departmental performance measures and how their employees can work towards achieving them. This is an ever evolving system and changes will be made as PERF see how it works. This system is both quantitative as well as qualitative.

Ms. Ettensohn asked Mr. Henning if it is just figuring out the measurements and setting expectations or is it an actual rewards system that includes increasing salaries or some monetary bonus system. Mr. Henning replied that he is working on getting metrics in place first. Once they are understood by the PERF staff the compensation dollars will follow. This compensation will be in base pay. Currently, almost everyone in a department doing similar work is being paid the same within a small range. Allowing people to start moving and differentiating themselves based on what they are able to do is the first step. Down the road PERF can look at other possibilities, but Mr. Henning thinks this basic program is one that PERF should do first.

Mr. Schalliol added that the Governor's general approach towards performance pay is to get the state aligned on their performance standards.

Mr. Adams emphasized how important this new process will be at PERF. He added that PERF is beginning to see individuals bring ideas forward for improvement. One example is the 'Wage & Contributions/Last Day in Pay Status' form that is now broken into two separate processes. It was individual employees who came forward with the idea of this to change to process to pay people faster. In the past they were told not to bring ideas to managers.

X. Executive Director Report

Mr. Adams updated the board on first quarter fiscal year 2006 accomplishments.

Mr. Adams indicated that \$1,025,000 in recurring savings have been identified and \$156,000 in one time savings since March 2005. The plan realized a 4.34% change in fund performance during the quarter. From a customer service standpoint, performance improved in member record processing (27%) retirement processing (15%) and customer satisfaction (5%). It was noted that refund processing time increased 5%. Mr. Adams discussed that the focus during the first quarter has been on improving the retirement processing function. A new measure was also identified, the average number of days from retirement to first check. Mr. Adams indicated that PERF has determined that this is the most critical measure for retirees.

Some of the Q1 highlights that were discussed with the board were

- Scorecard development and the customer surveys and focus groups that went into their development.
- Operations defined the 'as-is' environment, provided monthly comprehensive financial reporting and developed a service credit management process
- Customer service initiatives focused on developing a 'bridge to retirement' program, significant rewrites of forms and documents, prototyping of a 'annual wage and service summary' and creation of a customer exception management program
- Personnel resulting in the hiring of a CFO, CTO, Director of External Affairs and Director of benefits, the creation and implementation of a supplemental staffing program, monthly awards program and recruitment of a human resources manager to focus on performance management

- Technology enhancements include the formation of a data integrity group, facilities planning, system enhancements and replacements and web based developments
- Provided a customer testimonial from both an employer and a former members family.

Mr. Adams asked Mr. Huffman to demonstrate the new 'PERF Interactive' capabilities that was launched on November 14. This is new functionality and the first self-service functionality launched by PERF

Mr. Huffman walked the board through a demonstration of the new PERF Interactive features. Employers will now be able to change member addresses, investment options, beneficiary information and certify service credit online. Employees will be able to change their address, beneficiary, beneficiaries address, investment options and view their statements online. To make sure the site is secure members will have to sign up on the PERF website, create a User ID and Password, answer a few questions and then they will receive a pin number in the mail. Once they have received that they will have access to their information. There are less complex ways of doing this, but PERF felt the additional security was a must.

PERF also found buried in a change request log that IU wanted to work with them to take their personnel system and link it with PERF's. That way whenever IU changed an employee's address, it will automatically send PERF the electronic file with the new address. PERF has made their system open now so that they can accept those kinds of files from any employer. Prior to yesterday the only way you can change an address at PERF was to get the form from the website or from the office and mail it to back PERF or drop it off.

Mr. Adams expressed that this is a significant initiative for PERF. Change of address and investment forms may seem like trivial items, but represent 10-12 thousand monthly transactions for PERF. Not only does this provide good service to the customer but also frees up capacity at PERF to work on other issues.

Mr. Huffman also added that PERF has now built the technical infrastructure so that additional functionality and content will be added in the future.

Mr. Adams stated that the PERF website will evolve with additional content that is important to assisting future retirees with planning their own retirement.

XI. Date of Next Meeting

December 16th at noon.

XII. Adjournment

Meeting adjourned at 3:38pm.